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Italy – Summer 2013 Tax Developments Affecting Individuals

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There have been several notable tax developments over the past few weeks in Italy, despite August being a month during which Italians traditionally head to the beach. In this *Flash International Executive Alert*, we report on three important issues: the Fiscal Monitoring Regime's relaxation of penalties, the elimination of the Municipal Real Estate Tax, and the issuance of a circular by the Italian tax authority detailing further measures to prevent tax evasion.

Relaxation of Penalty System for the Foreign Asset Monitoring Return

On August 20, 2013, the Italian Parliament approved a package of measures,[1] the so-called "European Law," to rectify Italian laws that were potentially in violation of European Union law. Among these were measures designed to soften the penalties associated with the Foreign Asset Monitoring Return (Form RW)[2]. However, while relaxing the penalties for mis-reporting (more on this below), the government has broadened the scope of individuals who are obligated to complete the form (more on this below). Under existing Italian law, all Italian tax residents are required to report all assets with a minimum value of €10,000 (this has now changed as noted below) outside of Italy on Form RW, which is filed along with the Italian tax return by September 30th each year. Such assets include real estate, financial investments, bank accounts, precious metals, art-work, luxury automobiles, and yachts. This requirement applies not only to income-producing assets, but also to assets capable of producing future income or gains.

The Fiscal Monitoring Regime also requires Italian tax residents to report cash or investment transfers from Italy to foreign states, foreign states to Italy, and between foreign states. Any violation or mis-reporting under the Fiscal Monitoring Regime was punishable by a strict penalty of (in theory) up to 50 percent of the asset value and potential forfeiture of the assets. The European Commission (EU Pilot 1711/11/Tax) became concerned that this potential penalty regime was disproportionate to the deemed offense. In addition, there was further concern that taxpayers were being penalized for bank-to-bank transfer errors that had already been properly reported through the banking system.

As a result, the Italian government has softened the penalties applied in relation to Form RW and relaxed the reporting requirements for bank-to-bank transfers. Due to these new provisions, the penalty for individuals who incorrectly report on Form RW is reduced to between 3 percent and 15 percent of the value of the amount omitted. And if any error or omission is corrected within 90 days after the tax return deadline, the penalty is fixed at €258. In order to satisfy the European Commission's request, the Italian legislature revoked the obligation for individuals to complete Sections I and III of Form RW related to bank-to-bank and other transfers to and from abroad; taxpayers will no be longer be obligated to complete these sections. Section II remains on Form RW for reporting the total value of foreign assets held on December 31st of the fiscal year. Although the penalties for incorrect reporting of assets held in most countries were reduced, the penalties regarding incorrect reporting of assets held in "tax privileged" countries have been doubled.[3]

However, the government seems to have taken advantage of the changes in Form RW to eliminate the €10,000 reporting limit. As a result, it appears that individuals will have to report all foreign assets, even where minimal amounts are held.

KPMG Note

Any attempt to simplify Form RW is welcomed, especially the relaxation in duplicate reporting of bank-to-bank transfers. The relaxation in penalties should encourage more people to accurately report foreign assets without the fear of disproportionate penalties. Although this relaxation of the penalty rules is welcomed, further clarification regarding the valuation of certain non-financial assets would help prevent missreporting and establish a *de minimis* limit.

The abolition of the €10,000 reporting threshold seems to be a conservative step, bringing more people within the reporting requirement (even if they have a miniscule amount held outside Italy). For example, an individual who used to work in Germany, and still has a German bank account with minimal funds, would now have to report this amount.

Partial Elimination of Municipal Real Estate Tax

On August 31, 2013, Italy eliminated the municipal real estate tax (IMU) for the 2013 fiscal year.[4] However, it will be replaced by the so-called "service tax," which enters into force in 2014.

IMU is a controversial tax introduced in 2012[5] that applies to all proprieties owned, and it is calculated on the cadastral value of these properties and their type (i.e., principle residence, holiday home, etc.).

The first IMU payments for 2013 were suspended in May 2013, and due to new measures, the tax has been eliminated for principal residences and agricultural land. It is anticipated that the tax will be fully eliminated in 2014.

For now, home-owners will not pay IMU for 2013 in respect to the following real estate:

- Principal residence (excluding stately homes, villas, castles, and buildings of historic or artistic interest);
- Agricultural lands and rural properties.

Therefore, second or holiday homes continue to be subject to IMU for 2013.

KPMG Note

<u>Future Scenarios</u>

Although IMU will continue in 2014, it is anticipated that the lost revenues from it will be made up by a local tax on services (that is, the social and other local services provided in a given locality). The intent is to reorganize the real estate tax system to effectively tax the services connected with the property, as is typical in many European countries. One of the consequences will be the taxation of the real user of the house, not the home-owner; this would have an impact on rented houses.

Future Scenarios (cont'd)

In fact, if the proposed legislation is introduced, then the burden of the charge will be shifted to the tenant (rather than the home-owner).

Impact on International Assignees

In the case of international assignees who are provided with accommodation in Italy, the introduction of a services tax and shifting of the tax burden to the occupant (rather than the owner) may lead to an increase in costs. At the moment, tenants are only liable to pay rent, condominium charges, and a refuse tax. But going forward, they could also be responsible for increased service charges and extra accommodation costs.

Increased Measures Against Tax Evasion

In a circular issued on July 31, 2013,[6] the Italian Tax Agency (Agenzia delle Entrate) spelled out its strategy for fighting tax evasion and highlighted specific measures that might affect international assignees and Italians moving abroad. Specifically, this circular targets:

- Italians claiming to have a "fictitious" residence abroad;
- Foreigners working in Italy who are not known to the tax authorities.

The Tax Agency details its intention to use its new software, "SONORE," to provide the data that will allow the Agency to identify "high risk" individuals in both the above categories. The software searches existing tax databases (i.e., purchase records, rental registrations, vehicle registrations, and utility bills) to identify high risk individuals. Given that most transactions in Italy require a *codice fiscale,* there is already a means of linking such transactions. Therefore, individuals working in Italy and not paying taxes, along with Italians claiming to be residents abroad, could be identified from these records.

From an international perspective, it is understood that the SONORE software will be used to analyze data supplied to the Italian authorities by foreign tax authorities. For example, it could be used to identify an Italian tax resident individual who has purchased a property in France or opened a bank account in Spain.

The authorities also anticipate making greater use of data gathered from Italian banks and intermediaries regarding funds transferred to and from Italy.

The result of this effort could be an assessment notice from the tax authority with interest and penalties.

KPMG Note

The actions by the Italian tax authorities should not cause concern for international assignees who are legally registered in Italy and filing Italian tax returns. However, there may be some enquiries regarding individuals who may not have filed a return for legitimate reasons (i.e., exemption from Italian tax under an applicable double taxation treaty), but whose names have turned up because they rented property in Italy. The measures may also lead to some further enquiries regarding money

KPMG Note (cont'd)

transfers, which are unlikely to lead anywhere if there was correct reporting. Those foreign nationals living in Italy without proper tax documentation should make sure they are compliant with minimal delay.

The key message for all clients is to continue to disclose all foreign assets and bank accounts to prevent unnecessary enquiries being opened up.

Footnotes:

1 Legge 97/2013 – *Gazzetta Ufficiale* N. 194, 20 Agosto 2013.

2 Article 4 and 5 decreto legge 167/1990.

3 Among more common destinations for international assignees, the list of countries includes; Bahrain, the UAE, Isle of Man, Jersey, Guernsey, Hong Kong, Monaco, Switzerland, and Taiwan. The full list is published at:

http://www.agenziaentrate.gov.it/wps/content/Nsilib/Nsi/Documentazione/Fiscalita+internazionale/Black+list/Black+list+in+vigore+dal+19+febbraio+2002/ .

4 DL N. 102/2013 – *Gazzetta Ufficiale* N. 204. 31 Agosto 2013 – Supplemento Ordinario N. 66.

5 Legge N. 214/201.

6 Agenzia delle Entrate, Circolare N.25/E, 31 Luglio 2013.

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The information contained in this newsletter was submitted by the KPMG International member firm in Italy. The information contained herein is of a general nature and based on authorities that are subject to change. Applicability of the information to specific situations should be determined through consultation with your tax adviser.

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